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8 SEP 1974

MEMORANDUM FOR: Mr. Raymond J. Albright
Vice President
Planning and Research
Export-Import Bank of the United
States

SUBJECT : Eastern Europe: Indebtedness to
the West in 1980

Attached are the estimates and projections of Eastern Europe's trade and indebtedness with the West, which you requested in connection with your review of the Export-Import Bank's role in financing US exports to Eastern Europe.

MAURICE C. ERNST
Director
Economic Research

Attachment:
as stated

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(30 Aug 74)

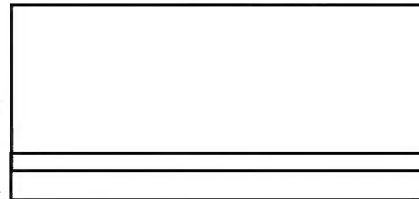
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Eastern Europe: Indebtedness to the West in 1980

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Eastern Europe: Indebtedness to the West in 1980

We project Eastern Europe's* indebtedness to the Industrial West** at \$38.5 billion at yearend 1980 compared with \$10.4 billion at yearend 1973. The additional \$28 billion in debt -- which includes short-term as well as medium- and long-term debt -- represents the cumulative current account deficits likely to be incurred in 1974-80 (Table 1). The principal assumptions underlying the projections are:

- . Exports in each country will grow in the same general pattern as in 1964-73, with a somewhat higher rate of increase in export prices;

- . Imports will continue to exceed exports by a substantial margin, with the actual amount of imports governed by the assumption that the debt service ratio in 1980 will be 40% for each country except Hungary; and

- . Interest payments for all debt will average 8% annually.

Indebtedness

East European indebtedness to the West in 1973 was estimated by updating estimates for each country, prepared by

for the Joint

* Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, and Romania.

** Australia, Austria, Belgium, Luxembourg, Canada, Denmark, Finland, France, Iceland, Ireland, Italy, Japan, the Netherlands, New Zealand, Norway, Sweden, Switzerland, United Kingdom, United States, and West Germany.

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Table 1

Eastern Europe: Estimated Indebtedness
to the Industrial West a/

	Estimated Indebtedness Yearend 1973	Cumulative Current Account Deficits 1974-80	Millions of \$US <u>a/</u> Implied Indebtedness Yearend 1980 <u>b/</u>
Total	10,361	28,117	38,478
Bulgaria	837	1,256	2,093
Czechoslovakia	1,478	3,164	4,642
East Germany	1,861	3,262	5,123
Hungary	1,130	4,971	6,101
Poland	2,726 <u>b/</u>	8,049	10,775 <u>c/</u>
Romania	2,329	7,415	9,744

a. Data include short-term as well as medium- and long-term indebtedness. The last two digits in the numbers are not significant and are presented only to facilitate further computations. The exchange rates used in arriving at these estimates were the official rates prevailing in July 1973.

b. Including \$300 million owed on PL-480 credits.

c. Including \$200 million owed on PL-480 credits.

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Congressional Economic Committee.* The indebtedness figures for 1980 were obtained by projecting exports, imports, and other current account items, as described below. Short-term debt was included in the overall indebtedness figures because of its rising importance in the East European indebtedness structure.

The resulting estimates of the debt structure and repayments for each country are based on fragmentary data and far-ranging assumptions; thus the figures are only tentative guides to the future.

Exports

The growth of East European exports to the West in 1974-80 (Tables 2 and 3) was estimated by using a semi-log projection of trends by country in 1964-73. The projections allowed for a 7% annual price rise -- higher than the estimated 5% annual rise in 1964-73.

Imports

The level of imports for each country was based on its capacity to import, as derived from the assumption that by 1980 all countries except Hungary would have a 40% debt service ratio (principal and interest on medium- and long-term debt to the West as a percentage of export earnings from the West).

* "Eastern Europe's Trade and Payments With the Industrial West," in Joint Economic Committee, US Congress, Reorientation and Commercial Relations of the Economies of Eastern Europe, Washington, USGPO, 16 August 1974, pp. 682-724.

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Table 2

Eastern Europe: Average Annual Growth Rates of Exports to,
and Imports from, the Industrial West

	Exports		Imports	
	Percent		Percent	
	1964-73 ^a /	Projected 1974-80	1964-73 ^a /	Projected 1974-80
Total	15	16	18	14
Bulgaria	15	14	14	17
Czechoslovakia	13	14	16	12
East Germany	12	13	17	9
Hungary	17	16	16	18
Poland	16	15	21	7
Romania	20	20	19	23

a. Based on East European data.

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Table 3

Eastern Europe: Value of Exports to, and
Imports from, the Industrial West ^{a/}

	<u>Millions of \$US^{b/}</u>	
	<u>1973 ^{c/}</u>	<u>Projected 1980</u>
Exports, total	7,793	21,582
Bulgaria	400	1,008
Czechoslovakia	1,274	3,212
East Germany	1,448	3,448
Hungary	1,261 ^{d/}	3,521
Poland	2,063	5,566
Romania	1,347	4,827
Imports, total	10,288	24,724
Bulgaria	466	1,374
Czechoslovakia	1,516	3,460
East Germany	2,004	3,665
Hungary	1,340 ^{d/}	4,269
Poland	3,431	5,582
Romania	1,531	6,374

a. Based on East European data.

b. Exchange rates prevailing in July 1973.

c. Data are preliminary except for Poland.

d. The Hungarians now report trade data on a country-of-origin and destination basis. These have been adjusted to a country-of-payments basis to make them comparable with earlier years.

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This results in a sharp reduction in the growth rate for those countries -- Poland and East Germany -- having large trade deficits in 1973. Actual debt service ceilings, however, will depend on individual country policy. Bulgaria and Romania, for example, approached the 50% level in 1972 but sizable gains in exports in 1973 reduced their debt service ratios to about 40%. In contrast, Hungary sharply cut the growth of imports from the Industrial West in 1972 when its debt service level had risen to only 25%; a debt service ratio of 22% was used in projecting Hungary's imports.

During 1974-80, Poland and Romania -- both especially eager to import Western technology -- may allow their debt service ratios to exceed 40%. The Poles in particular apparently are confident that imported machinery will generate compensating exports. If, for example, Poland boosted the growth of its exports to 17% a year and permitted a 50% debt service ratio, imports could grow at 12% a year, assuming a constant rate of growth. Poland's indebtedness under these circumstances would be \$15.9 billion instead of the \$10.8 billion of Table 1.

Some Limitations of the Projections

Except for Poland and East Germany, the projections indicate that East European exports to the West will grow

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rapidly enough through 1980 to provide imports required to sustain growth. Poland will have to restrict the growth of imports sharply in 1974-80 to stay within the 40% or even a 50% limit -- unless it can boost the growth rate of exports far above the assumed 15%.

Perhaps the most important factor not considered in the projections is the impact of the increased dependence of Eastern Europe on high-priced Western crude oil, which requires hard currency payments. By 1980, Eastern Europe may have to obtain one-third to two-fifths of its oil imports from the Middle East compared with 15% in 1973. Although the East Europeans are seeking barter deals, they probably will have to pay for a considerable share of this oil in hard currency at higher prices than in 1973. Furthermore, Soviet oil prices almost certainly will rise, starting in 1976, to conform more closely to world market levels. Bulgaria will be by far the hardest hit, followed by Czechoslovakia, East Germany, and Hungary. Poland still relies heavily on coal to satisfy domestic energy requirements, and Romania is a net oil exporter. Even with Soviet and Western assistance, most East European countries will not be able to avoid strains on their balance of payments and on their domestic economies in 1976-80. The rising

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fuel bills are likely to result in reductions of imports of consumer manufactures and raw materials for domestic chemical industries.

The projections also do not take into account: (1) the ability of the West to absorb increased East European goods; (2) the potentially sharp fluctuations in agricultural production; (3) changes in the commodity structure of foreign trade due to relative price changes; (4) the implications of restrictive Common Market policy toward agricultural commodities; and (5) the flexibility of the West in its financial arrangements, such as in supplying longer term credits, refinancing outstanding credits, and engaging in new cooperative ventures, including equity ventures.